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SUBJECT: DAS BRYZA'S JANUARY 14 MEETING WITH TOP
AZERBAIJANI OFFICIALS ON ENERGY SECURITY

Classified By: EUR A/S Dan Fried for Reasons 1.4 (B) and (D)

¶1. (C) Summary: EUR On the margins of Nagorno-Karabakh discussions, DAS Matt Bryza discussed energy security on January 14 in Baku with State Oil Company of the Azerbaijan Republic (SOCAR) President Rovnaq Abdullayev, President Aliyev, and Foreign Minister Mammadyarov. Bryza briefed the three Azerbaijani officials on Turkish President Gul's recent visit to Washington and the improved relations between the USG and GOT -- including on energy security -- as a result of improved U.S.-Turkey collaboration against PKK terrorists. On Azerbaijan's gas transit agreement with Turkey, Abdullayev said SOCAR was still unwilling to agree to Turkey retaining the right to reserve any volume of gas -- no matter how small. But President Aliyev indicated separately to Bryza the GOAJ was willing to compromise and could agree to Turkey reserving a "small percentage" at a slightly discounted price. FM Mammadyarov stressed it was now time to press Turkmenistan to agree to the interconnection of its Livanov natural gas field with Azerbaijan's existing infrastructure in the Caspian Sea to provide more gas for the Southern Corridor, following the first meeting of the Azerbaijan-Turkmenistan Inter-Governmental Commission the previous week. End Summary.

¶2. (C) DAS Bryza briefed President Aliyev, FM Mammadyarov, and SOCAR President Abdullayev on President Gul's visit to Washington, noting that Turkey displayed a new eagerness to advance strategic cooperation on energy security and other issues now that cooperation with the U.S. against PKK terrorists had improved significantly. DAS Bryza told Mammadyarov and Abdullayev that Energy Minister Guler now sought to identify a joint action plan with a specific timeline for advancing the Southern Corridor with gas from Azerbaijan and Turkmenistan.

¶3. (C) Abdullayev welcomed the idea of enhanced cooperation with the U.S. and Turkey to realize TGI and Nabucco with gas from Azerbaijan and Turkmenistan. He said SOCAR wanted to reach an agreement with Turkey on gas transit, but could not agree to Turkey's demand to reserve 15 percent of the gas flowing through the TGI pipeline at the netback price paid by Italy. He lamented that if each country participating in the Nabucco project demanded a 15 percent reserve at a discounted price, Azerbaijan would be obligated to expand gas exports dramatically at such a low price as to leave Azerbaijan with virtually no profit. Abdullayev warned that in April, SOCAR

would seek equalize Turkey,s purchase price of gas from the Shah Deniz field with the price Turkey currently pays Gazprom. A free market approach to setting prices made more economic sense than reserved prices.

¶4. (C) In a separate meeting, President Aliyev indicated Azerbaijan was more willing to compromise with Turkey. President Aliyev told DAS Bryza Azerbaijan could agree to Turkey reserving a smaller percentage (perhaps 5 percent) of gas flowing into TGI at a price perhaps a bit lower than what Turkey pays Russia. (Comment: Turkish Energy Minister Guler told Bryza the previous week in Washington that Turkey might be able to agree to these same terms. End Comment.)

¶4. (C) Abdullayev cautioned that Russia was pushing South Stream as an alternative to TGI and Nabucco. Russia,s approach was deterring European partners from committing to gas sales/purchase agreements with Azerbaijan. DAS Abdullayev lamented that European governments were not committing themselves to invest in Nabucco. Bryza said that European governments were not yet ready to embrace Nabucco because they thought private companies could develop it on their own. Bryza opined that one way to convince Allies to get behind the project was to offer reciprocal take-or-pay, or ship-or-pay, clauses. Abdullayev told Bryza the second phase of Shah Deniz development would yield 12-16 bcm of gas, which would guarantee Nabucco,s profitability (Embassy Baku Comment: BP projections for Shah Deniz Phase Two are more conservative than those of SOCAR. End Comment). Abdullayev said he had told Austrian firm and Nabucco lead developer OMV that SOCAR was ready to conclude a gas sales/purchase agreement for 4 bcm for Nabucco immediately, (or half of the 8 BCM required to Nabucco,s first phase, but that in return SOCAR wanted to be a 20 percent partner in the project (Embassy Baku Comment: OMV has previously offered SOCAR part ownership in Nabucco. End Comment). Abdullayev opined that OMV hostile takeover bid of its Nabucco partner, Hungarian energy company MOL, was also hampering Nabucco,s advance. Bryza promised to encourage OMV CEO Wolfgang Ruttenstorfer and Nabucco Project Manager Reinhard Mitschek to engage SOCAR on a ship-or-pay/take-or-pay contract for Azerbaijani gas.

¶5. (C) Abdullayev said Greece was raising concerns that Azerbaijan didn,t have enough gas to fill Nabucco. This was false, since Azerbaijan has nearly 3 trillion cubic meters of gas reserves. However, Greece wanted good relations with Russia and was thus distorting the true quantities of Azerbaijan,s reserves. Abdullayev said that, in the first phase of development of the TGI pipeline, SOCAR could guarantee 2 BCM, but once it had reached an agreement on gas storage to resolve seasonal differences in supply, it could guarantee 5 BCM, with higher volumes in coming years.

¶6. (C) Abdullayev warned that, if Russia increased its gas price, Turkmenistan might lose interest in selling gas to Western Europe through the Southern Corridor. Abdullayev said he had recently been to Turkmenistan to try to convince the GOTX of the profitability of the South Caspian pipeline and had promised clear and transparent tariffs. Bryza agreed with SOCAR,s approach, saying that clear and transparent tariffs would be a form of insurance for Turkmenistan. Regarding the disputed Kyapaz/Serdar oil field, Abdullayev said BP and Chevron had already contacted the GOTX to help mediate a solution. Abdullayev said that SOCAR had proposed a 50-50 ownership deal if its infrastructure were used to develop Kyapaz/Serdar, but indicated Azerbaijan would be willing to settle for 40 percent of Kyapaz/Serdar. Abdullayev concluded by telling Bryza there was a need to combine energy discussions in Europe and the Caspian region. He recommended that Bryza serve as the lead U.S. negotiator to ensure both Caspian suppliers and European consumers were working toward the same goal.

¶7. (C) Foreign Minister Mammadyarov had a more optimistic view of cooperation with Turkmenistan. He noted the first

session of the Azerbaijan-Turkmenistan Inter-Governmental Commission had concluded successfully the previous week. Turkmenistani President Berdimukhamedov had demonstrated his "strong support" for inter-connecting gas production at Turkmenistan's Livanov Field in the Caspian Sea with Azerbaijan's existing natural gas export infrastructure just 60 km away in the Caspian. The two countries were also moving closer on Caspian delimitation, having agreed on the median line method to demarcate their maritime boundary. In a break from his previous, more cautious position, FM Mammadyarov encouraged the U.S. to urge Turkmenistan to move ahead with the gas interconnection in the Caspian Sea, even before final agreement is reached on Caspian demarcation. Mammadyarov expressed confidence the demarcation discussions would make progress over time, but did not wish to wait to develop the gas interconnection. FM Mammadyarov also reiterated his strong support for a ministerial-level conference that could be convened by the European Union in Brussels on Nabucco and Azerbaijan/Turkmenistan gas supplies.

(Embassy Baku Comment: In a subsequent meeting with Ambassador Derse, FM Mammadyarov promoted the idea of an EU Summit, vice EU Ministerial conference, as only a summit would be high-level enough to guarantee the participation of GOTX President Berdimukhamedov. End Comment).

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